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Oil and Gas Leasing of Idaho Farm and Ranch Land

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I. Introduction

A farmer or rancher whose land might contain an oil or gas deposit may enter any of several development arrangements with an oil and gas explorer and producer. By far the most common arrangement is a lease. This bulletin discusses the legal rights and duties of a farmer or rancher who enters into an oil and gas lease. It will be assumed that the farmer or rancher owns both the surface and the mineral rights at the time of leasing. This excludes cases where ownership of the surface and the mineral estates has been severed before leasing.[1]

Oil and gas law is a complex subject. Multi-volume treatises have been written about it. Oil and gas leases cannot be treated comprehensively in a brief bulletin. The topics selected for discussion here were chosen either because they are basic to the structure of an oil and gas lease or because they are of special concern to a farmer or rancher. The discussion is necessarily general and should not be viewed as a substitute for legal advice. Because slight changes in fact situations may require a material variance in the legal result, the advice of an attorney should be sought regarding particular situations. The assistance of an attorney may be valuable both before and after a lease is signed. Before leasing, the attorney can answer questions and review the lease offered by the mineral developer to determine whether any modifications would be advisable for the client's particular needs. After leasing, the attorney can assist in the resolution of legal problems that may arise.

Oil and gas leasing was rare in Idaho for many years. For that reason there is a lack of Idaho law regarding such leases. The discussion in this bulletin is based upon the law of states with established oil and gas industries. An Idaho court is very likely to follow legal principles that have wide acceptance in such states. When those states are not in agreement upon a particular legal point, prediction of what an Idaho court would do is, of course, difficult.

II. Is There A Standard Lease?

The parties to a lease are called the lessor and the lessee. The lessor is the landowner who is leasing his land or some rights in it to another. The lessee is the person to whom the land is leased. Thus, the farmer or rancher who signs an oil and gas lease would be the lessor, and the oil company or developer would be the lessee.

The legal rights and duties of an oil and gas lessor depend in large part upon the terms of the lease he signs. Many oil and gas leases offered to farmers and ranchers are printed forms bearing the designation "Producers 88 Lease." The Producers 88 was an early form of lease characterized by brevity and simplicity, which came to be widely used and readily accepted by landowners. In time, various difficulties and deficiencies in the form became apparent, and regular users of the form came to add various clauses of their own. As a result, estimates are that there are now over 200 varieties of Producers 88 Lease.

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[1] Among the situations excluded, therefore, are those in which a farmer or rancher acquired the land subject to a reservation of mineral rights by the federal government and then the government leased the oil and gas rights to a mineral developer. The farmer or rancher would not be a party to such a lease. His concerns are likely to center around surface use and water rights conflicts. In general the legal principles regarding surface and water rights discussed in sections VI and VII of this bulletin would be applicable. The rights of a farmer or rancher in a particular case, however, may depend also upon the terms of the federal land grant statute under which his land was patented, other federal statutes, and the terms of the oil and gas developer's lease. Federal oil and gas lease form 4-213 requires the lessee to take reasonable steps to prevent soil erosion, water pollution, and damage to crops or improvements of the surface owner; upon conclusion of operations, the lessee may be required, so far as reasonably can be done, to restore the surface to its former condition.

While there is no single standard oil and gas lease, there is a definitely recognizable uniformity among lease forms. The discussion which follows will refer to typical lease clauses. These clauses are standard components of modern oil and gas leases. This is not to say, however, that there is no variation from one lease to the next in the specific language or even the scope of such clauses. Nor should it be understood that the clauses discussed are the only ones which are standard.

III. What Minerals Are Covered by the Lease?

An oil and gas lease will list the minerals which are the subject of the lease. The lease may, for example, entitle the lessee to explore for and produce "oil and gas," or "oil and gas and other hydrocarbons," or "oil and gas and all other minerals." The first phrase quoted is, of course, the narrowest. The courts of different states are in disagreement as to whether "other minerals" in the third phrase should be limited to petroleum substances or should include a broad range of minerals. Even the second phrase may be ambiguous as to whether it includes not only liquid but solid hydrocarbons such as coal. Many landowners prefer to lease only for those minerals the lessee demands and retain rights to all other minerals for possible later leasing for an additional bonus or rental. Another advantage to the landowner in this approach is that the lessee's right to use the surface for exploration is restricted to fewer minerals.

IV. How Long Will the Lease Last?

A number of provisions in an oil and gas lease determine its duration. The term or habendum clause sets the basic structure, but length is also affected by the drilling and rental clause and by various savings clauses.

> **Typical term clause:** *It is agreed that this lease shall remain in force for a term of ________ years from this date, and as long thereafter as oil and gas, or either of them, is produced from said land by the lessee, its successors and assigns.*

The typical term clause establishes a primary term of fixed duration plus a secondary term of indefinite length which depends upon the production of oil or gas. The primary term is subject to negotiation, but 3, 5, or 10 year terms are the most common. There has been considerable litigation in oil and gas states regarding what constitutes "production" for the purposes of extending the lease beyond the primary term and continuing it during the secondary term. The production requirement generally has been interpreted to mean production in paying quantities, which in turn has been construed to mean that the lessee must have a profit after deducting current operating expenses and marketing costs. He need not deduct any portion of drilling costs for this purpose. There is disagreement about some items such as whether depreciation must be deducted as an operating expense. In determining whether the requisite production in paying quantities is present, profitability must be computed over a reasonable period of time.

> **Typical drilling and rental clause:** *If no well be commenced on said land on or before ____, 19____, this lease shall terminate as to both parties unless the lessee on or before that date shall pay or tender to the lessor or the lessor's credit in the ____________ Bank at ________, or its successors, which shall continue as the depository regardless of changes in the ownership of said land, the sum of ________ dollars, which shall operate as a rental and cover the privilege of deferring the commencement of a well for ________ months from said date. In like manner and upon like payments or tenders, the commencement of a well may be further deferred for like periods of the same number of months successively. And it is understood and agreed that the consideration first recited herein, the down payment, covers not only the privileges granted to the date when said first rental is payable, as aforesaid, but also the lessee's option of extending that period as aforesaid, and all other rights conferred.*

Even though the primary term is for a fixed duration such as 10 years, the lease will not necessarily last that long. The drilling and rental clause requires that at various specified intervals, such as every 12 months, the lessee must either have commenced a well or, in lieu thereof, paid a delay rental. If the lessee does neither, the lease terminates even though the primary term has not yet run its course. The primary term fixes the time beyond which the lease may not be continued by the payment of a delay rental.

The drilling and rental clause makes the commencement of a well a significant event and has produced a lot of litigation about what constitutes commencement. Actual drilling is not necessary. Certain preparatory steps will suffice if the lessee manifests the intent to carry through and complete the well.

Together the term clause and the drilling and rental clause serve reasonably well to satisfy the desires and interests of lessors and lessees. The landowner-lessor is assured that either: (1) there will be prompt exploration, or (2) he will receive delay rentals, or (3) the lease will terminate and he will be free to lease the land to another for mineral development if he wishes. The lessee is able to tie up land for the primary term without obligation to engage in expensive exploration and with assurance of being able to continue the lease after the primary term if commercial production is obtained. The two clauses alone, however, fail to resolve certain difficulties of particular concern to lessees. While lessees have prevailed in litigation perhaps more often than not in these matters, various savings clauses designed to reduce a lessee's risks regarding durational disputes have become standard features in oil and gas leases.

Miscellaneous Savings Clauses

Typical drilling operations clause: *Lessee shall have the right to drill to completion with reasonable diligence and dispatch any well commenced within the term of this lease. If oil or gas or either of them be found in paying quantities in any such well, this lease shall continue and be in force with like effect as if such well had been completed within the term of years herein first mentioned.*

Suppose a lessee is in the middle of drilling a well when the primary term ends and there is no other producing well on the leased land. The lessee continues drilling and obtains a producing well. Does the farmer or rancher hold the land free of the lease because there was no production at the end of the primary term as required by the term clause? Courts have divided on this issue, and it has never been resolved in some states. The drilling operations clause is intended to protect the lessee in such a situation. A variation, called a continuous drilling operations clause, enables a lessee to preserve the lease by continuous drilling operations which lead to a producing well even though the producer is a different well from the one which was partially completed at the end of the primary term.

Typical dry hole clause: *If any well drilled on the land described above prior to discovery of oil or gas should be a dry hole and if additional drilling is not commenced before the next ensuing rental-paying date after the expiration of 90 days from the date of such dry hole, this lease shall terminate as to both parties unless the lessee, on or before the rental-paying date next ensuing after the expiration of 90 days from the date of completion of the dry hole, shall resume the payment of rentals in the same amount and in the same manner as hereinbefore provided; and it is agreed that upon resumption of the payment of rentals as above provided, this lease shall continue in force as though there had been no interruption in the rental payment. If a dry hole should be drilled at any time subsequent to 90 days prior to the beginning of the last year of the primary term, no rental payment is necessary to keep this lease in force during the remainder of the primary term.*

Suppose the lessee commences a well during the primary term but abandons it as a dry hole. If he does not commence another well with reasonable promptness does the lease terminate by abandonment or can he continue the lease by paying delay rentals? If he can continue it, when is the next delay rental due? The dry hole clause is intended to provide answers to these questions.

Typical cessation of production clause: *If any well drilled on the land described above should cease to produce and there is no other producing well on the land and drilling operations are not being conducted thereon, and if additional drilling is not commenced before the next ensuing rental-paying date after the expiration of 90 days from the date of the cessation of production, this lease shall terminate as to both parties unless the lessee, on or before the rental-paying date next ensuing after the expiration of 90 days from the date of the cessation of production, shall resume the payment of rentals in the same amount and in the same manner as hereinbefore provided; and it is agreed that upon resumption of the payment of rentals as above provided, this lease shall continue in force as though there had been no interruption in the rental payment. If production ceases at any time subsequent to 90 days prior to the beginning of the last year of the primary term, no rental payment or operations are necessary in order to keep this lease in force during the remainder of the primary term. If, after the expiration of the primary term hereof, production shall cease from any cause, this lease shall not terminate if lessee resumes operations for the drilling of a well or restoration of production within 90 days from such cessation, and this lease shall remain in force and effect during the prosecution of such operations and, if production results therefrom, then as long thereafter as such production continues.*

Suppose production in paying quantities ceases for a prolonged period due to some reason other than exhaustion of the supply in the ground, e.g., governmental regulation, breakdown of equipment, or a decline in market price. This could happen during either the primary or the secondary term. If it happens during the primary term, can the lessee still keep the lease in force without having to commence drilling a new well or pay a delay rental? If it happens during the secondary term, does the lease terminate for lack of production? The cessation of production clause is intended to clarify the positions of the parties in these situations.

Typical shut-in royalty clause: *If at any time, either before or after the expiration of the primary term of this lease, there is any gas well on the lands covered hereby, or on other lands with which said lands are pooled or unitized, which is capable of producing in* *paying quantities, but which is shut-in either before or after production therefrom, and the production therefrom is not being sold or used, lessee agrees to pay or tender to the mineral owners in the depository bank named in the lease, as royalty, a sum equal to the amount of delay rentals under this lease. Such payments shall be made on or before the shut-in royalty payment date, as herein defined, next accruing after the expiration of 90 days from the date such well was shut-in, unless prior to such date gas from the well is produced and sold or used. In like manner, on or before each succeeding shut-in royalty payment date while such gas well remains shut-in, lessee shall make payment of shut-in gas royalty in the same amount and manner. A shut-in gas well capable of producing in paying quantities shall be considered under all provisions of this lease as a producing well and this lease shall be in force and effect in like manner as though the gas therefrom were actually being produced and sold or used. The term "shut-in royalty payment date" shall mean any rental paying date of this lease if within the primary term, or any subsequent anniversary thereof if after the primary term.*

Suppose the lessee discovers gas but is unable to market it due to lack of access to a pipe line facility. Under the great weight of authority, the lease will not extend beyond the primary term even though the only reason for nonproduction is the lack of a pipe line. The shut-in royalty clause is designed to enable a lessee in such a situation to continue the lease in force indefinitely by the payment of a sum of money. Shut-in royalty clauses vary in scope; the one quoted above appears to cover any number of reasons why a well capable of production is not producing, e.g., a decision by the operator that it is inadvisable to produce for the time being. If so, it could overlap with the cessation of production clause, although it would be unnecessary to determine which governs unless the payments due under the two clauses are different in amount or the right to receive payments had been assigned to different persons.

V. What Compensation Will or Might the Landowner Receive?

In return for giving the lessee the right to explore for and produce oil and gas, the landowner typically receives, or potentially may receive, three types of compensation.

(1) **Bonus**. This is usually a cash payment stated in terms of so many dollars per acre which is paid when the lease is signed. Sometimes the bonus may take the form of a share of production in addition to the usual landowner's royalty.

(2) **Delay Rental**. This is a sum of money usually stated in terms of so many dollars per acre which is to be paid periodically, such as annually, by the lessee during the primary term of the lease for the privilege of deferring the commencement of drilling operations.

(3) **Royalty**. This is a share of production paid to the landowner whenever oil or gas is produced from the premises. In most oil-producing regions of the country, the landowner's royalty traditionally has been one-eighth of production.

Typical landowner's royalty clause: *In consideration of the premises the lessee convenants and agrees:*

First, the lessee shall deliver to the credit of lessor as royalty, free of cost in the pipe line to which lessee may connect its wells, the equal 1/8 part of all oil produced and saved from the leased premises, or, at lessee's option, may buy or sell such 1/8 royalty and pay lessor the market price of oil of like grade and gravity prevailing in the field on the day such oil is run into pipe lines or into storage tanks.

Second. To pay lessor 1/8 of the proceeds received for gas sold from each well where gas only is found, or the market value at the well of such gas used off the premises, and lessor to have gas free of cost from any well for all stoves and all inside lights in the principal dwelling house on such land during the same time by making his own connections with the well at his own risk and expense.

Third. To pay lessor 1/8 of the market value at the well for gas produced from any oil well and used off the premises, or for the manufacture of casing-head gasoline or dry commercial gas.

The clause set forth above has three parts — an oil royalty provision, a gas royalty provision, and a royalty provision for casing-head (or wet) gas from an oil well from which gasoline may be extracted. The oil royalty clause, unlike the other two, authorizes payment of the royalty either in kind (i.e., by delivery of the royalty oil to the credit of the lessor in the pipe line) or in money based on the market value of the oil. The physical properties of gas make delivery in kind more difficult, and gas royalty clauses usually provide only for payment in money.

The oil royalty clause speaks of delivery to the credit of the lessor "free of cost in the pipe line." The other clauses speak of money payments based on market value at the well. Such language generally has been construed to mean that the lessor receives his share free of costs of production such as the expense of geophysical surveys, drilling, and testing and completing the well. The royalty is not free of expenses subsequent to production, such as gross production or severence taxes and costs of transporting the oil or gas to the buyer.

In almost all states, the lessee's failure to make a royalty payment is not grounds for cancellation of the lease absent an express forfeiture clause.

The second provision of the royalty clause quoted above contains a free gas clause, under this the lessor is allowed to take gas from a producing well for certain domestic purposes. Free gas clauses are fairly common. Not so common, but perhaps desirable for many farmer-lessors, is a so-called irrigation gas clause, under which the lessor is entitled to receive at an agreed price such gas as is needed to operate pumps for irrigation purposes.

Although analysis of the federal income tax depletion allowance is beyond the scope of this bulletin, it might be noted in passing that bonus and royalty payments are subject to the depletion allowance while delay rental payments are not.

VI. What Are the Rights of the Parties to the Lease to Use the Surface of the Land?

Lessee's Rights

> **Typical granting clause:** *Lessor grants and leases unto the lessee, its successors, and assigns (certain land) for the purposes of surveying by geological, geophysical, and all other methods, mining and operating for oil and gas, laying pipe lines, building tanks, power stations, and other structures thereon to produce, save, and take care of said products.*

The granting clause of an oil and gas lease typically enumerates the purposes for which the land is leased. The lessee has an implied right to make reasonable use of the surface of the leased land necessary to accomplish those purposes without liability to the landowner for damages. Even without a detailed enumeration of purposes, an oil and gas lessee generally has an implied right to make any use of the surface reasonably necessary to oil and gas exploration and development. The implied right of surface use can, of course, be enlarged or diminished by appropriate lease clauses. Without protective lease provisions, however, the lessor has no legal remedy for damage to crops, livestock, improvements, or the land itself unless the lessee uses more land than reasonably necessary or, though not using excess land, is negligent in his conduct. Sometimes a lessee will pay for surface damage, even though not legally obligated to do so, in order to maintain amicable relations with the surface owner.

A lessee's implied right to make reasonable use of the surface is said to give him the dominant estate in the land and leave the lessor with the servient estate. A number of courts have added that although the lessee has the dominant estate, he must exercise his right of surface use with due regard to the rights of the surface owner. It is not clear just what that means, except that it does not give the landowner as much protection as a literal interpretation might suggest. Most cases, for example, have given the lessee great latitude to select the time and place for drilling, even though another time or place would cause less crop or other damage, so long as the lessee acts in good faith. Also, the prevailing view seems to be that a lessee has no duty to fence off his immediate operating area and thus has no liability for livestock who "trespass" into such area and are injured by the machinery, by falling into pits, or by drinking oil.

A recent Texas case may be of interest to Idaho farmer-lessors. The surface owner in that case had a self-propelled sprinkler irrigation system supported by a series of towers that rotated around a pivot point. Subsequently the lessee located two oil wells within the irrigated area, and the wells utilized beam-type pumping units that were too high to enable the sprinkler pipe to rotate. The court ruled the lessee's use of airspace was limited to that which was reasonably necessary and upheld a jury finding that it was not reasonably necessary for the lessee to use so much airspace. The beam-type pumps could have been recessed in cellars or lower hydraulic pumps could have been used without causing interference with the irrigation system.

This case notwithstanding, it should be clear that a landowner is much better off to have specific protective clauses in the lease than to rely on the concepts that the lessee's use of the surface must be reasonably necessary and must be exercised with due regard to the rights of the surface owner. In a given case these concepts may provide either no protection or protection which is established only after litigation.

> **Other typical surface use clauses:** *When requested by lessor, lessee shall bury lessee's pipe lines below plow depth. No well shall be drilled nearer than 200 feet to the house or barn now on said premises without the written consent of lessor. Lessee shall pay for damages caused by lessee's operations on said land. Lessee shall have the right at any time to remove all machinery and fixtures placed on said premises, including the right to draw and remove casing.*

The first three clauses above are examples of common provisions protecting the lessor's surface estate. The pipe line clause puts the initiative on the lessor to make timely request for burial. A recent Kansas case held, however, that an identically worded clause imposed a continuing duty upon the lessee to keep pipe lines buried deeply enough to allow for normally anticipated agricultural practices. Thus, the lessee had to pay for re-burying pipe lines to a depth that permitted terracing by the landowner. The damage liability clause above appears to be broadly drafted. Some such clauses cover only growing crops. In that event if there are no other protective clauses in the lease, the lessee would not be liable for nonnegligent injury to livestock, improvements, or the land itself as a result of reasonably necessary activities. Also, the phrase "growing crops" is unclear with respect to such questions as whether native grasses and trees are included.

Another matter of concern to a landowner is restoration of the surface after exploration or development operations cease. The general rule, again absent a contrary lease clause, is that the lessee has no duty to restore the premises to their prior condition if the lessee's activities have not gone beyond reasonably necessary use. This rule has been eroded in recent items by some judicial decisions requiring the lessee during the continuance of the lease to fill pits and remove obstructions as the need for them ceases and by surface restoration statutes enacted in some states. The Idaho Surface Mining Act has no application to oil and gas operations.

Lessor's Rights

An oil and gas lessor can continue to use the surface in any manner not prohibited by lease provision so long as the lessee has no need to use the surface. Unless the lessor is protected by an appropriate damage clause, however, he runs the risk that crops he plants or improvements he makes will be subsequently damaged by prudent operations of the lessee without liability. The lessor must yield possession of the surface to the lessee as the latter requires it for lease purposes under the test of reasonable need.

Rights of Agricultural Lessee

A landowner who executes an oil and gas lease may also lease the surface of the land to a third person for agricultural use. The oil and gas lease may be executed either before or after the agricultural lease. In either event, surface use conflicts may arise between the two lessees. If the oil and gas lease was executed first, the agricultural lessee takes possession subject to the reasonable use rights of the oil and gas lessee. If the agricultural lease came first, case authority for resolving surface use conflicts is meager and lacking in consistency.

VII. How Will the Lease Affect the Landowner's Water Rights?

Lessee's Use of Water

Typical free water clause: *Lessee shall have the right to use, free of cost, gas, oil, and water produced on said land for its operations thereon, except water from wells and reservoirs of lessor.*

As a corollary of the implied right to make reasonable use of the surface of the leased land, a lessee may take and use water from the land that is reasonably necessary for oil and gas operations. The free water clause above confirms that right but makes it clear that the right does not extend to water from the lessor's wells and reservoirs. Some free water clauses exclude only the lessor's wells. In that event courts in different jurisdictions have gone both ways on the question of whether the lessee may take water from private ponds of the lessor.

Modern oil production technology includes a secondary recovery technique called water flooding, in which water is injected into a partially depleted oil bearing formation in order to wash the oil out of the rock and into a well. Increased use of that technique is likely to increase water use conflicts between the lessor and the lessee. One can easily foresee an oil developer sinking a water well for water flooding purposes which interferes with the supply to the lessor's irrigation or domestic wells. There has been little litigation to date on this problem, however, and the eventual course of law is not clear.

A recent Texas decision on this matter has attracted considerable attention. The lessee in that case had an oil and gas lease containing a free water clause essentially the same as the one quoted above. When oil production from its wells on the leased land diminished, the lessee drilled a water flood well that used about 100,000 gallons of water per day. Prior to that time the lessor had sold the surface of the land, subject to the oil and gas lease, to a third person who was using the land for irrigated agriculture and drawing irrigation water from the same aquifer that supplied the water flooding well. The surface owner objected to the oil and gas lessee's water well. At trial the surface owner obtained damages and an injunction against further pumping by the lessee. The intermediate appellate court affirmed on the ground that the free water clause was ambiguous and the evidence supported the jury's conclusion that the lease did not contemplate the use of large quantities of water for water flooding. The Texas Supreme Court reversed and rendered judgment for the lessee, concluding in substance that: (1) the lessee had an implied right to use as much ground water from the land as may be reasonably necessary to produce oil; (2) the free water clause in the lease did not restrict that implied right except to prevent the lessee from using the lessor's wells; and (3) the lessee's use of water from its own well on the leased land for water flooding operations was reasonably necessary to effectuate the purposes of the lease.

The court's final conclusion was in direct rejection of a jury finding that use of the ground water from the lessee's well was not reasonably necessary to accomplish the purpose of the lease. Presumably the jury had been moved by evidence that while there was no other water source available to the lessee on the leased land, the necessary water could have been purchased from outside sources and that such purchase would have been economically feasible for the lessee. Moreover, the lessee's use of ground water was expected to shorten the life of the surface owner's water supply by at least 8 years (apparently from a projected life of about 40 years). The Texas Supreme Court reasoned, however, that to require the lessee to purchase water from other sources or owners of other tracts in the area would be in derogation of the dominant mineral estate. The decision is an eye-opening commentary upon the principle that a lessee's right of reasonable use of the leased land is limited by a requirement of due regard for the interests of the surface owner.

The impact of the Texas case in other jurisdictions is difficult to predict. The decision has been criticized by commentators. More importantly, the Texas law of ground water is quite different from the law of most western states, including Idaho. In Texas ground water is governed by the absolute ownership doctrine, under which a well owner has almost no protection against depletion of his water supply by another well. In a state like Idaho, which applies the appropriation doctrine to ground water, a landowner with an existing domestic or agricultural well ought to be protected against injury by an oil and gas lessee's junior well. The Idaho ground water act protects a senior appropriator in the maintenance of a reasonable ground water pumping level and prohibits the mining of ground water basins. It would seem that the lessee should be subject to these limitations in a suit by the landowner unless he could persuade the court that the lease gives rise not only to an implied right to make reasonably necessary use of the surface but also an implied covenant by the lessor not to sue for interference with water supply caused by reasonably necessary operations of the lessee.

The muddle just discussed can, of course, be avoided by an appropriate lease clause if the lessor is alert to it before signing the lease. The lessor might negotiate for a clause expressly prohibiting the use of water on or under the leased land for water flooding operations or for an even stronger clause to the effect that no use of water by the lessee shall interfere with the supply of water for the lessor's use in the present or in the future.

Pollution by Lessee

The Idaho Oil and Gas Conservation Act makes it unlawful for anyone to commence operations for the drilling of an oil or gas well without first obtaining a permit from the State Oil and Gas Conservation Commission. No permit may be issued until the Director of the Department of Water Resources has had an opportunity to recommend the inclusion of conditions he believes necessary to protect fresh water supplies. The act also empowers the Commission to regulate the disposal of salt water and oil-field wastes. The commission has issued regulations pursuant to that authority, e.g., the regulations prohibit the impounding of brine or salt water in earthen pits where the soil under the pit is porous and closely underlaid by a gravel or sand stratum.

Idaho statute makes it unlawful to construct or use a waste disposal and injection well without a permit from the Director of the Department of Water Resources. This legislation could include wells used for the subsurface disposal of wastes from oil and gas or other mineral operations. No permit may issue if the proposed well will unreasonably contaminate or deteriorate the ground water below quality standards adopted by the State Board of Health and Welfare or will affect the rights of others to use water for beneficial purposes. If a permit is granted it may contain certain conditions necessary to protect the public interest in the ground-water resource.

If an oil and gas lessee pollutes the lessor's water supply, the lessee may be held liable to the lessor if his conduct has breached a duty imposed by statute or administrative agency regulation or order. Even without a duty grounded in statute or agency regulation or order, a lessee may in certain circumstances be held liable upon a negligence theory for water pollution damage.

Landowner's Use of Lessee's Drilling

An oil and gas lessee might drill a well which fails to produce oil or gas but which is capable of providing water suitable for irrigation or domestic use. In such event the landowner may desire to have the use of the well. For that reason, occasionally an oil and gas lease will require the lessee to notify the lessor of all water-bearing strata encountered by the drill hole, and if the well is not a producer of oil or gas, to give the lessor the option to require the lessee to leave as much casing and tubing in place as required to use the well for water production.

VIII. What is Pooling?

Typical pooling clause: *Lessee is hereby granted the right and power to pool or combine the acreage covered by this lease or any portion thereof with other land, lease or leases in the vicinity thereof at any time and from time to time, whether before or after production, when in lessee's judgment it is necessary or advisable to do so for the prevention of waste and the conservation and greatest ultimate recovery of oil or gas. Such pooling shall be into a unit or units not exceeding in area the acreage prescribed by any lawful authority for the drilling or operation of the well, or 40 acres in each unit for the production of oil, or 640 acres in each unit for the production of gas, whichever is larger. Such pooling shall be effected by lessee's executing and filing in the office where this lease is recorded an instrument identifying and describing the pooled acreage. The production of pooled substances and development and operation on any portion of a unit so pooled, including the commencement, drilling, completion, and operation of a well thereon, shall be treated, for all purposes except the payment of royalty, as production,* *development, and operation on the leased premises. The royalties herein provided shall accrue and be paid to lessor on pooled substances produced from any unit in the proportion, but only in the proportion, that lessor's acreage interest in the land covered hereby and placed in the unit bears to the total acreage in the land placed in such unit.*

Pooling refers to the combining of separately owned small tracts into a larger sized drilling unit. In the early days of the oil industry derricks were constructed very close together in the race to recover oil, and great economic and physical waste resulted from drilling unnecessary wells. Most states, including Idaho, have now enacted conservation statutes which empower an administrative body to regulate the spacing of wells and production therefrom. Leases commonly contain pooling clauses to enable lessees to comply with spacing regulations or to hold leases under an efficiently designed spacing program. There is considerable variation among pooling clauses with respect to the circumstances under which the lessee is authorized to pool, the method of designating the pooled acreage, and the effect of production within the unit upon various other clauses in the lease.

The above pooling clause appears to create risks which many lessors would prefer to avoid. Suppose a farmer leases 640 acres for oil development and just one of those acres is included in a pooled 320-acre gas producing unit. The farmer or rancher would receive 1/320 of the 1/8 landowner's royalty. This small payment might excuse the lessee from paying any rental on the remaining 639 acres under lease but excluded from the pooled unit. If the gas well were shut-in for lack of a market, the lessee might be able to perpetuate the entire 640 acre lease by payment to the farmer of 1/320 of the amount prescribed by the shut-in royalty clause. Such risks to the farmer could, of course, be avoided by careful drafting of the pooling clause, e.g., it might provide in the event of partial pooling for a severance of the lease into separate leases for the pooled and unpooled acreage.

Although there are few cases in point, it would appear that a typical pooling clause enlarges the lessee's implied right to make reasonable use of the leased land (see VI and VII above) so that the lessee may use water from that land for the production of oil or gas from a well on other land included within a pooled unit. Conversely, the lessor on whose land the well is situated will be subject to a heavy burden of surface use; yet he will receive only a proportionate share of the royalties. He has particular need for a broadly drafted clause making the lessee liable for damage to the surface.

IX. Implied Covenants -- The Unwritten Rules of A Lease

The courts have held that an oil and gas lease impliedly obligates the lessee to do certain things. Among the more important implied covenants are duties: (1) to drill an initial well, (2) to protect against drainage of oil or gas from the leased premises by wells on adjoining land, (3) to develop the lease after production by drilling additional wells, (4) to produce and market the product, and (5) to use reasonable care in the conduct of operations. In most states compliance with these covenants is determined by a prudent operator standard, which means that the lessee must do what a reasonably prudent operator in the same or similar circumstances would have done to discharge the duty. Thus, the implied duty to protect the leased premises from drainage, for example, does not obligate the lessee to spend more to prevent drainage than the oil and gas saved would be worth.

Express lease provisions may negate the existence of implied covenants. For example, the modern drilling and rental clause negates the implied obligation to drill an initial exploratory well by giving the lessee the option of either drilling, paying a delay rental, or allowing the lease to terminate. The courts are divided on the question of whether the payment of a delay rental negates or diminishes the lessee's implied duty to protect against drainage. Payment under a shut-in royalty clause probably does not negate the lessee's implied duty to market, although there is a scarcity of case authority on this question.

The State is truly our campus. We desire to work for all citizens of the State striving to provide the best possible educational and research information and its application through Cooperative Extension in order to provide a high quality food supply, a strong economy for the State and a quality of life desired by all.

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Research ... Agricultural Research scientists are located at the campus in Moscow, at Research and Extension Centers near Aberdeen, Caldwell, Parma, Sandpoint, Tetonia, Twin Falls and at the U.S. Sheep Experiment Station, Dubois and the USDA/ARS Soil and Water Laboratory at Kimberly. Their work includes research on every major agricultural program in Idaho and on economic and community development activities that apply to the state as a whole.

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